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SUBJECT: Global Financial Slowdown Hits Egypt

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¶1. SUMMARY: During the fourth quarter of 2008, Egypt experienced a substantial downturn in its three main sources of revenue and foreign exchange: tourism, worker remittances and Suez Canal fees. Though the extent of the slowdown is yet unknown, the GOE suggests that Egypt could see a $5-6 billion decrease in revenue in 2009. End Summary.

¶2. Each of the top three sources of Egyptian revenue saw a sharp decrease in revenue during the last quarter of 2008. In an interview on January 14, Minister of Economic Development Osman Mohammed Osman estimated that Egypt could lose between $5-6 billion in foreign revenue in the 2009 year due to the global economic slowdown. In FY2007/2008 (July-June), tourism and worker remittances generated $10.9 billion and $8.56 billion, respectively. The Suez Canal, Egypt's third largest revenue producer, generated $5.2 billion during the same period, a steady increase over previous years.

¶3. Tourism is Egypt's largest source of revenue and directly or indirectly contributes to 11.3% of GDP. All tourism indicators have shown steady growth in recent years. Egypt's industry began to feel the impact of the global economic slowdown in the final quarter of 2008, after a good showing the rest of the year. The tourism industry grew by 25% in 2008, according to the Minister of Tourism, but the final quarter saw a decline of 17.8%. Hotel bookings were down 30% in 2008 compared to 2007 (ref A). More recently, the Gaza incursion has led to cancellations at Red Sea and Upper Egypt resorts from European and Israeli tourists. The GOE has attempted to implement some incentives, such as exempting hotels tourism promotion fees and reducing landing fees for charter flights, but we are not sure this will have a strong impact on the stagnant or downward trend we anticipate in 2009. Anecdotally, the manager of a major Cairo hotel told us occupancy is running at about 50%, whereas normally it would be more like 65-70%. Beltone Financial is more optimistic, however, projecting that tourism revenues in FY2008-09 will be roughly consistent with FY2007-08's $10.8 billion.

¶4. Remittances from Egyptians working abroad sustain millions of Egyptian families. The country is the sixth largest recipient of remittances among middle income countries. The Central Bank and the World Bank estimates that Egyptian expatriate workers sent home $8.56 billion in FY2007/2008, six percent of GDP. The U.S. was the largest single source of remittances, sending $2.8 billion in remittances in FY2007/2008, according to the Central Bank. Like tourism and Suez Canal revenues, remittances have been growing steady in recent years as the Gulf and Middle East economies generally, have been performing well. According to the Information and Decision Support Center (IDSC), the Egyptian Cabinet's think tank and polling unit, approximately 840,000 Egyptians work in Persian Gulf countries in construction, real estate, financial services and the medical sector. Economic analysts believe that the plummeting price of oil and the bursting of the real estate bubble in the Gulf could cause hundreds of thousands of Egyptian workers in the United Arab Emirates and other Gulf nations to lose their jobs. Sources differ about the overall impact on remittances in the coming year but several leading Egyptian economists speculated in the press

that remittances could drop at least 40%.

¶5. Revenue from Suez Canal transit fees accounted for $5.2 billion in FY2007/2008, 3.4% of GDP. However, the monthly numbers began to fall late in the year and December's revenues were $391.8 million, compared with $419.8 million in November, ending a seven year steady increase. On an annual basis, revenues still rose by 1.7%. Canal operations have been doubly hit by the combination of global economic slowdown and the rising threat of piracy in the Gulf of Aden (ref B). Suez Canal Authority (SCA) Chairman Ahmed Fadel told the press on January 12 that he expects a 7% decrease in overall traffic through the Canal in 2009 compared to 2008. Beltone Financial predicts the Canal will generate $4.9 billion in FY2008/2008, a slight drop from the $5.2 billion in the previous fiscal year. Fadel said that the SCA was holding transit fees steady at 2008 levels, but that he would consider price cuts if the economic downturn continued unabated. SCA is reportedly considering incentives and additional services to attract more traffic.

¶6. COMMENT: In recent years, Egypt's economy has become more diverse and better integrated into the global economy. Egypt has seen several years of strong growth, including 8% GDP growth in FY2007/8. Though the banking sector remains liquid and relatively unscathed from the crisis, the country is beginning to see the indirect impacts from the global slowdown. Lower global commodity prices may ease some of the stress on Egypt's fiscal spending, but lower export revenues, decreased tourist flow, reduced income from worker remittances and the Suez Canal are likely to reduce overall growth (estimates are in the 4-5% range, compared with the 7-8% in the last three years). The expected drop in revenue will likely limit the GOE's ability to mitigate the domestic impact of the financial crisis and impair planned infrastructure development and other economic priorities. The GOE is already planning on 15 billion pounds (US$ 2.7b) in spending to stimulate the economy. Finance Minister Boutros Ghali remains a deficit hawk, and does not want to lose gains in recent years in curbing the deficit.

¶7. COMMENT CONT'D: In addition to the impact on revenues, if there are significant layoffs of Egyptian workers in the Gulf, the GOE faces the possibility of those workers returning to Egypt to look for work, adding to the ranks of the unemployed. Unskilled workers are plentiful in Egypt and are not likely to find employment, putting additional stress on an already inadequate social safety net. Over the past two-three years, during the economic boom, many companies complained they were unable to find or retain skilled workers, so skilled workers returning from the Gulf may be able to find jobs at these firms as the economic crisis eases.
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